Office - Supreme Court, U.S
FILED
FEB 29 1984
ALEXANDER L. STEVAS
CLERK

No. 83-297

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

ARMCO, INC.,

Appellant

v.

DAVID C. HARDESTY, JR.,
STATE TAX COMMISSIONER OF WEST VIRGINIA,

Appellee

On Appeal from the Supreme Court of Appeals of West Virginia

BRIEF FOR THE NATIONAL CONFERENCE OF STATE LEGISLATURES, THE COUNCIL OF STATE GOVERNMENTS, THE NATIONAL LEAGUE OF CITIES, THE INTERNATIONAL CITY MANAGEMENT ASSOCIATION, AND THE NATIONAL ASSOCIATION OF COUNTIES AS AMICI CURIAE IN SUPPORT OF THE APPELLEE

LAWRENCE R. VELVEL *
Chief Counsel
ELAINE D. KAPLAN
Attorney
State and Local Legal Center
444 North Capitol Street, NW
Suite 349
Washington, D.C. 20001
(202) 638-1445

STEFAN F. TUCKER
JOSEPH G. HOWE, III
TUCKER, FLYER, SANGER & LEWIS
1730 Massachusetts Avenue, NW
Washington, D.C. 20036
Counsel for the *Amici Curiae*

* Counsel of Record

WILSON - EPES PRINTING CO., INC. - 789-0096 - WASHINGTON, D.C. 20001

QUESTION PRESENTED

Whether it is constitutional for a state to tax sales to in-state customers by large companies that conduct extensive in-state marketing activities which give rise to the very sales being taxed, and that also perform other crucial aspects of their integrated operations within the state.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
TABLE OF CONTENTS	iii
TABLE OF AUTHORITIES	v
INTEREST OF THE AMICI CURIAE	1
STATEMENT OF THE CASE	3
SUMMARY OF ARGUMENT	6
ARGUMENT	10
I. West Virginia Possesses The Constitutional Power To Tax Armco's Wholesale Sales To Customers Located In West Virginia	10
A. A State Can Impose a Tax Where the Requisite Nexus Exists and the Taxpayer is Obtaining Benefits From the State	10
B. The Requisite Nexus Exists Because Armco Engages in Purposive Revenue Generating Activities in West Virginia, Activities Which Create the Market for the Products it Sells to Customers Within the State	10
C. Armco Obtains the Benefits and Protection Offered by the State	11
D. The West Virginia Tax is Constitutional Under this Court's Decision in *Standard Pressed Steel Co. v. Washington Department of Revenue*	12
E. Public Policy Supports the West Virginia Tax	14

TABLE OF CONTENTS—Continued

Page

F. West Virginia's Tax on Sales to West Virginia Customers is Constitutional Because Armco is a Unitary Enterprise Which Performs a Crucial Aspect of its Integrated Business Activities Inside the State 15

II. The West Virginia System of Taxation Is Fair And Nondiscriminatory 17

A. Introduction 17

B. Well Established Principles Govern Armco's Claim 17

C. The West Virginia Tax System is Lawful Under the Foregoing Principles 18

D. The Validity of West Virginia's Tax System is Supported by Decisions of This Court..... 21

CONCLUSION 22

TABLE OF AUTHORITIES

CASES — Page

Alaska v. Arctic Maid, 366 U.S. 199 (1961) 21
Caskey Baking Co. v. Virginia, 313 U.S. 117 (1941) 21
Container Corporation of America v. Franchise Tax Board, —— U.S. ——, 102 S. Ct. 2933 (1983) 8, 16, 18
Exxon Corporation v. Wisconsin Department of Revenue, 447 U.S. 207 (1980) 16
Gregg Dyeing Co. v. Query, 286 U.S. 472 (1932) ....
Gwin, White & Prince v. Henneford, 305 U.S. 434 (1939) 10, 20
Halliburton Oil Well Co. v. Reily, 373 U.S. 64 (1963) 17, 18
Norton Co. v. Department of Revenue, 340 U.S. 534 (1951) 13, 14, 18
Postal Telegraph-Cable Co. v. Richmond, 249 U.S. 252 (1919) 10
Standard Pressed Steel Co. v. Washington Department of Revenue, 419 U.S. 560 (1975) 6, 7, 10, 12, 13, 14, 20
Washington v. United States, —— U.S. ——, 103 S. Ct. 1344 (1983) 17, 18

STATUTES

W. Va. Code § 11-13-2b 19

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

No. 83-297

ARMCO, INC.,

Appellant

v.

DAVID C. HARDESTY, JR.,
STATE TAX COMMISSIONER OF WEST VIRGINIA,

Appellee

On Appeal from the Supreme Court of Appeals of West Virginia

BRIEF FOR THE NATIONAL CONFERENCE OF STATE LEGISLATURES, THE COUNCIL OF STATE GOVERNMENTS, THE NATIONAL LEAGUE OF CITIES, THE INTERNATIONAL CITY MANAGEMENT ASSOCIATION, AND THE NATIONAL ASSOCIATION OF COUNTIES AS AMICI CURIAE IN SUPPORT OF THE APPELLEE

INTEREST OF THE AMICI CURIAE

The *amici* are organizations that represent state and local governments located throughout the United States. *Amici* and their members have a vital interest in legal

questions affecting such governments. This case presents an issue of great importance concerning the taxing authority of state governments. For it raises the question whether a state may tax sales to in-state customers by companies that conduct extensive in-state marketing activities which give rise to the very sales being taxed, and that also perform other crucial aspects of their integrated operations within the state.

In prior cases this Court has recognized that "interstate commerce must pay its way," by bearing its fair share of local tax burdens, when companies involved in such commerce engage in business activity within a state and enjoy benefits and protections provided by the state. Continued adherence to this established principle is crucial in this case. There are two reasons.

First, it has become common for companies to do business within a state by engaging there in significant activities which create a market for the companies' products, or by performing other crucial aspects of integrated operations there. By doing business within a state in these ways, companies secure the benefits and protections offered by the state.

Second, financially hard-pressed states must have access to justified sources of revenue necessary to fund the very benefits and protections obtained by companies which do business within their borders. If a state cannot tax sales to in-state customers when market-creating or other vital activities are performed in-state, then it will be denied essential revenues. Concomitantly, large national companies will be able to engage in extensive in-state activities, and obtain benefits and protections from the state, without paying their appropriate share of state taxes.

Thus, a ruling that a state can tax in-state sales stemming from in-state activities is necessary to avoid imposing an unfair fiscal burden on state governments. *Amici*

are therefore submitting this brief to assist the Court in its consideration of this litigation.[1]

STATEMENT OF THE CASE[2]

1. Armco, Inc., is a vertically integrated Ohio corporation that does business in West Virginia and other states (App. 3a). It is engaged in the business of manufacturing and selling steel products (*id.* at 39a). For this purpose it mines coal, manufactures steel, fabricates finished steel products, and distributes the products to wholesalers and end users (*id.* at 3a-4a; 39a). It has at least four mines in West Virginia at which it extracts, cleans and processes the coal used in the manufacture of its steel (*id.* at 3a). Its finished products are sold to customers located in West Virginia and elsewhere (*id.* at 3a-4a).

Armco is organized into divisions, including the Mining Division, the Steel Group, the Union Wire Rope Division, and the Metal Products Division. Various divisions conduct sales, promotional and marketing activities within West Virginia (App. 3a-4a). The Steel Group promotes sales of its products to West Virginia customers by sending each of four salesmen into West Virginia on virtually a monthly basis to solicit orders from customers located in the state. The salesmen are available to give advice concerning Armco's line of products and to make recommendations regarding a customer's needs. They tailor orders to the customer's specifications and forward the orders to Armco's offices. They make follow-up calls on customers to check whether the products have been satisfactory, and occasionally investigate complaints and service the products (*ibid.*).

---

[1] Pursuant to Rule 36, the parties have consented to the filing of this *amicus* brief. Their letters of consent have been lodged with the Clerk of the Court.

[2] References to the Appendix filed with Appellant's Jurisdictional Statement shall be noted as App. ——.

The activities of the Union Wire Rope Division in West Virginia are similar. It has three salesmen who visit West Virginia customers once or twice a month to solicit orders. The salesmen make follow-up calls to check customer satisfaction, investigate complaints, and service products (App. 4a).

The Metal Products Division maintains an office at South Charleston, West Virginia, where it employs two sales engineers (App. 4a). This office solicits the sale in West Virginia of all of the division's products except metal buildings. Such buildings are sold by Armco franchisees who reside in West Virginia and are authorized to use the corporation's name, trademarks and advertisements (*ibid.*). Armco shares advertising expenses with the local franchisees, and the franchisees and Armco have agreed to close cooperation for the "development and mutual growth of their individual businesses" (App. 4a; 49a).

2. West Virginia imposes a business and occupation tax of .88 percent on the value of tangible property manufactured within the state. It also imposes a business and occupation tax at the much lesser rate of .25 percent upon gross receipts realized from wholesale sales of tangible property by persons doing business within the state. The wholesale sales tax is forgiven if the taxpayer has previously paid the manufacturing tax, whose percentage rate is, of course, three and one half times that of the wholesale sales tax (App. 19a-20a).

3. This case arises out of Armco's failure to pay the appropriate amount of tax during a six-year period, 1970-1975. During that time Armco understated and failed to pay taxes due on its coal operations in West Virginia, and failed to pay any tax on sales made to West Virginia customers by its Steel Products Group, its Union Wire Rope Division, and the metal buildings subgroup of its Metal Products Division (App. 38a-39a).

The Tax Commissioner of West Virginia issued on assessment against Armco for the taxes owing. At a hearing, Armco conceded it owed certain portions of the tax on its coal operations and was found to owe other portions (App. 39a; 44a-47a). However, it claimed the state could not tax the sales made to West Virginia customers by the Steel Group, the Union Wire Rope Division, or the metal buildings subgroup (*id.* at 47a-49a).

The hearing examiner rejected Armco's claim, ruling that West Virginia can tax these sales because there is a nexus with the state. In this regard, the examiner found that salesmen for the Steel Group and the Union Wire Rope Division carry on marketing activities within the state in "a systematic and repetitive manner", and that such activities are "crucial to the development and maintenance of a market for the taxpayer's product in this state" (App. 48a). He also pointed out that the metal buildings subgroup uses and engages in activities with local franchisees, and found that these actions are "designed to hold a market for the taxpayer's product" by insuring that the franchisees have a resale market (*id.* at 49a).

Armco thereafter appealed to a state trial court which overturned the prior decision. It ruled that the sales by the Steel Group, the Union Wire Rope Division and the metal buildings subgroup were not taxable because there was not a sufficient nexus with the state (App. 26a-31a).

The state then took the case to the West Virginia Supreme Court, which reversed the trial court. The state supreme court held that Armco's divisions are part of "a unitary business corporation conducting its business activity under one corporate umbrella," and ruled that Armco's in-state sales and coal mining activities establish a nexus with the state that justifies imposition of the tax (App. 14a-15a).

The state supreme court also concluded that, because the tax is assessed in proportion to Armco's activities in

West Virginia, it is fairly apportioned and bears a rational relationship to the services and benefits conferred upon Armco by the state (App. 15a-19a).

Finally, the court ruled that the wholesale sales tax does not discriminate against out-of-state manufacturers. Rather, when West Virginia's tax laws are viewed as a whole, out-of-state manufacturers who make wholesale sales to West Virginia customers, and pay the wholesale sales tax, bear a lighter tax burden than in-state manufacturers who pay the manufacturing tax (App. 19a-23a).

SUMMARY OF ARGUMENT

I.

A. West Virginia possesses the constitutional power to tax Armco's wholesale sales to customers located in the state. For there is a nexus with the state and Armco receives protection and benefits from the state.

A nexus exists because Armco engages within the state in a host of purposive revenue generating activities that create the very sales being taxed. These activities include regular and frequent visits to customers by Armco salesmen to solicit sales and follow-up afterwards. They also include the presence and activities of Armco's local franchisees.

Armco obtains benefits and protections from West Virginia because of the in-state presence and activities of its salesmen, franchisees, and coal mines. It uses the state's roads, receives police and fire protection, has access to local courts to enforce its contracts, and secures the advantages of state laws and policies that foster a business climate in which there is a market for its products.

B. West Virginia's power to tax Armco's wholesale sales to in-state customers is dispositively supported by this Court's decision in *Standard Pressed Steel Co. v. Washington Department of Revenue*, 419 U.S. 560

(1975). In that case a tax imposed by Washington on a Pennsylvania company was upheld because the taxpayer had one employee who, working out of his home, consulted with the taxpayer's lone Washington customer to determine the latter's anticipated needs and follow up on any difficulties. The Court ruled the tax constitutional because the employee "made possible the realization and continuance of valuable contractual relations" between the taxpayer and the customer. 419 U.S. at 562. Here Armco's numerous salesmen and franchisees likewise "ma[k]e possible the realization and continuance of valuable contractual relations" between Armco and customers.

The only difference in the two cases is that the lone employee in *Standard Pressed Steel* lived in Washington, whereas here Armco's numerous salesmen (though not its franchisees) live out-of-state. But their place of residence is irrelevant because their activities occur within West Virginia and Armco obtains benefits and protection from the state.

C. Sound reasons of public policy also support West Virginia's authority to tax Armco's sales. Face to face sales efforts intended to generate a market for a producer's goods are a vital component of modern business practice, and are engaged in by tens of thousands of companies. If a state cannot tax the sales to local customers generated by such in-state sales efforts, then one of the major activities of modern business will not serve as a basis for taxation of business.

Preclusion of this basis of taxation would be as wrong in principle as precluding manufacturing from being a basis of taxation, since both activities are major components of the commercial and industrial process. Preclusion would also cause financially hard pressed state governments to be cut off from a well justified source of revenue.

D. Armco's wholesale sales to West Virginia customers can also be taxed because Armco is a unitary, vertically

integrated business enterprise whose ultimate goal is the sale of finished steel products. One of the major components of this unitary enterprise—the mining and processing of coal—occurs within West Virginia, and the state can therefore tax the sale to West Virginia customers of the end product of the unitary enterprise. The state is merely taxing the in-state consummation of a unitary series of activities that in important part occurred within the state.

II.

A. Armco claims that West Virginia's wholesale tax discriminates against interstate commerce. The claim is wrong. The state's tax is a fair and non-discriminatory one which comports with decisions of this Court. To the extent it gives an advantage to anyone, the advantage goes not to in-state manufacturers who sell to West Virginia customers, but to companies like Armco which manufacture products out-of-state and sell them to customers located in West Virginia.

Well established principles govern Armco's claim of discrimination. To begin with, the Court has repeatedly ruled that, in considering a claim of discrimination, the state's whole scheme of taxation must be taken into account. The Court has also held that a claim of discrimination must be judged on a practical dollars and cents basis, not on the basis of legal abstractions. In this regard it has pointed out that a party is not the victim of discrimination when it is better off than other taxpayers because it pays the state less tax than they. Finally, the Court has ruled that, when a taxpayer claims discrimination, it bears the "distinct burden" of proving the claim by "clear and cogent evidence." *Container Corporation of America v. Franchise Tax Board*, —— U.S. ——, ——, 103 S.Ct. 2933, 2939-40 (1983).

Under these principles, West Virginia's tax is plainly nondiscriminatory and constitutional. The state imposes a tax at the rate of .88 percent on the manufactured value of products made in the state, and a tax at the far

lower rate of .25 percent on tangible goods sold at wholesale to West Virginia customers. The wholesale tax is forgiven if the goods were manufactured in-state and subjected to the manufacturing tax.

Because the wholesale tax is assessed at a far lower percentage rate than the manufacturing tax, an out-of-state producer such as Armco, which is subject to the wholesale but not the manufacturing tax, will normally pay less money to the state than would be paid if its goods were produced in-state and subjected to the manufacturing tax but not the wholesale tax. Thus, when the system is viewed as a whole, companies like Armco which manufacture products out-of-state will normally be better off on an actual dollars and cents basis than if their goods were made in-state.

Armco has not even alleged, let alone tried to prove by clear and cogent evidence, that the actual facts of the case are any different than this. Thus it has not even claimed it pays more tax to the state under the .25 percent wholesale tax rate than would be paid under the .88 percent manufacturing tax rate.

Nor has Armco even alleged, let alone tried to prove, that in actual fact it suffers discrimination because of the combined effects of the West Virginia wholesale tax plus some manufacturing tax in Ohio, where it produces its goods. In other words, it has not even claimed that, because of any such combined effect, it in fact pays a greater sum in total manufacturing and wholesale sales taxes than would be paid if its goods were manufactured in West Virginia. Rather than even allege this, it merely presents hypothetical speculations on what the situation *might* be *if* Ohio imposed a tax. But hypothetical speculations are not the "clear and cogent evidence" required for a taxpayer to carry its "distinct burden" of proving unconstitutional discrimination. Were it otherwise, the taxing power of financially hard pressed states would be crippled by hypothetical arguments lacking any basis in fact.

ARGUMENT

I. WEST VIRGINIA POSSESSES THE CONSTITUTIONAL POWER TO TAX ARMCO'S WHOLESALE SALES TO CUSTOMERS LOCATED IN WEST VIRGINIA

A. A State Can Impose a Tax Where the Requisite Nexus Exists And the Taxpayer Is Obtaining Benefits From the State

The question in this case is whether West Virginia can tax wholesale sales made by Armco to customers located within the state. The question turns on two interrelated principles established in this Court's decisions on whether state taxes are lawful under the interstate commerce and due process clauses. The first is that a state can tax a company's in-state sales when there is an appropriate nexus between the state on the one hand and the company and its activities on the other. *E.g., Standard Pressed Steel Co. v. Department of Revenue of Washington*, 419 U.S. 560, 562-563 (1975). The second is that, when it engages in commercial activity within a state and benefits from the advantages offered by the state, " 'even interstate commerce must pay its way' by bearing its share of local tax burdens." *Gwin, White & Prince v. Henneford*, 305 U.S. 434, 438 (1939), quoting *Postal Telegraph-Cable Co. v. Richmond*, 249 U.S. 252, 259 (1919). In this case both of these interrelated principles are easily satisfied.

B. The Requisite Nexus Exists Because Armco Engages In Purposive Revenue Generating Activities in West Virginia, Activities Which Create the Market for the Products It Sells to Customers Within the State

In this case Armco engages in a host of purposive revenue generating activities within West Virginia. These activities prominently include regular, frequent and active solicitation by Armco salesmen of the very sales the state is taxing. By means of such solicitations, which are essential in selling steel products, Armco is physically

present in and doing business in West Virginia for the purpose of systematically creating a market for its goods. Armco's activities in West Virginia thus create the nexus necessary to support taxation.

Armco's Steel Division sends each of four salesmen into the state on virtually a monthly basis to solicit sales which are the subject of the West Virginia tax. In addition representatives from the Steel Division investigate complaints and occasionally perform service work in connection with the Division's products. The Union Wire Rope Division also sends its salesmen into the state to solicit orders: three salesmen visit customers in West Virginia once or twice a month for this purpose. These salesmen also follow up the sales to verify customer satisfaction with the products.

The Metal Products Division, which maintains a West Virginia office with salemen who visit customers located throughout the state, sells its metal buildings through local franchisees whom it has licensed to use the corporate name, trademarks and advertising, and with whom it shares advertising expenses. It also cooperates closely with these franchisees in order to strengthen the sale of its products.

In these ways Armco is physically doing business in West Virginia for the purpose of generating the sales which are the subject of the tax. In addition, Armco engages in major in-state activities which are essential to its ability to manufacture the products it sells to West Virginia customers. Specifically, it mines, cleans and ships huge amounts of West Virginia coal which it uses to make the steel for the products it sells to customers in the state.

C. Armco Obtains the Benefits and Protection Offered by the State

By virtue of its regular frequent presence in West Virginia to generate sales, its presence there through franchisees licensed to use its marks and advertising, and its

extensive activities relating to coal, Armco obtains the benefits and protection offered by the state. It uses the state's roads, is protected by the state's police and fire departments, has access to the state's courts to enforce its contracts, and secures the advantages offered by state laws and policies which foster a business climate in which steel products are sold. In paying a wholesale tax on sales to West Virginia customers, Armco is simply paying a very small share of the taxes necessary to support the benefits it obtains.

D. The West Virginia Tax Is Constitutional Under This Court's Decision In *Standard Pressed Steel Co. v. Washington Department of Revenue*

The decision of this Court in *Standard Pressed Steel Co. v. Washington Department of Revenue, supra*, lends dispositive support to West Virginia's position. For *Standard Pressed Steel* establishes that a state can levy a gross receipts tax when in-state activities contribute to the sales on which the tax is imposed.

In the *Standard Pressed Steel* case, the state of Washington levied a gross receipts tax on sales of aerospace fasteners by the taxpayer to its sole Washington customer, the Boeing Company. The taxpayer, Standard, had no office in Washington, and Boeing sent orders directly to Standard's out-of-state home office. The orders were also filled out-of-state, with the product being sent directly to Boeing via common carrier. Payment was made directly to Standard. Standard's commercial interests with Boeing were looked after by an in-state employee, one Martinson, who operated out of his home. This employee "consult[ed] with Boeing regarding its anticipated needs and requirements for aerospace fasteners and . . . follow[ed] up any difficulties in the use of appellant's product after it was delivered." 419 U.S. at 561.

In these circumstances, Standard argued that the tax on its gross receipts was unconstitutional because its

contacts with Washington were "so thin and inconsequential" that the tax had "no reasonable relation to the protection and benefits conferred by the taxing state." 419 U.S. at 562. The Court, however, thought the taxpayer's argument "verge[d] on the frivolous" because Martinson's activities within the state "made possible the realization and continuance of valuable contractual relations between [Standard] and Boeing." *Ibid.*

The present case is virtually identical to the *Standard Pressed Steel* case. For the activities of Armco salesmen and franchisees within West Virginia "ma[ke] possible the realization and continuance of valuable contractual relations" between Armco and its customers. The only difference in the two cases is that Standard's single relevant employee lived in Washington, whereas Armco's numerous relevant salesmen live outside West Virginia but enter it on a regular and frequent basis to discuss customers' needs, to take orders, and to follow up afterwards. (Armco's franchisees, of course, live in-state, as did Martinson.) But the salesmen's places of residence are irrelevant. For their pertinent *activities* occur within West Virginia and Armco thereby obtains the "protection and benefits conferred by the taxing state."

Armco, however, asserts that the decision in *Norton Co. v. Department of Revenue*, 340 U.S. 534 (1951), precludes imposition of West Virginia's tax. The same argument was made in *Standard Pressed Steel*, where the Court noted that "[m]uch reliance is placed on *Norton*." 419 U.S. at 562. The argument was rejected in *Standard Pressed Steel* and should be rejected here. As the Court pointed out in *Standard Pressed Steel*, the nontaxable sales in *Norton* involved orders that were sent directly from in-state customers to an out-of-state seller, were filled out-of-state, and were shipped directly to the customer. *Ibid.*; see *Norton*, *supra*, 340 U.S. at 538. Thus, there was no local in-state activity that could be the basis for a tax on these sales. Here, of course, the situation is

far different. For here Armco's salesmen and franchisees engage in regular and frequent in-state activities that serve as a predicate for the tax on the wholesale sales.[3]

E. Public Policy Supports the West Virginia Tax

Sound reasons of public policy support the principle, applied in *Standard Pressed Steel* and applicable here, that a state can tax sales to customers located within its boundaries when a company engages there in activities which generate the very sales being taxed.

Face to face sales efforts which generate a market for a producer's goods are not some trivial or incidental activity in the business world. Rather, they are a vital component of the crucial marketing efforts of scores of thousands of companies. They are, in fine, one of the major ways in which business is done. They are especially important to wholesale sales of industrial products, the type of sales being taxed here.

Because face to face sales and marketing efforts are crucial, and because of the ease of modern transportation, untold thousands of salesmen continuously and systematically visit "foreign" states of the Union to promote and secure orders for products. By virtue of their regular visits, their companies secure the benefits and protections offered by each of the "host" states, benefits and protections which are the same as those secured by Armco in this case. If the host states cannot tax sales

---

[3] This case is also much different from the old "drummer" cases. In those cases, as pointed out in *Norton*, the taxpayer could be viewed as "remote and inaccessible," and could not be reached with process for breach of contract or defective goods. 340 U.S. at 538. Armco is not remote and inaccessible. Rather it is continuously present at its customers' West Virginia premises through the regular visits of its salesmen, is also present in West Virginia through its licensed franchisees, and is present in the state through its coal mines. Furthermore, because of its presence in West Virginia, it can be reached with process.

generated by the in-state efforts of the salesmen, then one of the major commercial and industrial activities of modern American business will not serve as a basis for the exercise of a state's power to tax business.

To preclude in-state sales and marketing activities from being a basis of taxation would be as wrong in principle as precluding manufacturing from being a basis of taxation. The one, no less than the other, is a major component of the industrial and commercial process. In addition to being wrong in principle, the preclusion would be detrimental to the ability of state governments to raise the monies necessary to support the very benefits and protections offered to companies that send salesmen into the states to secure business. State governments, already hard pressed financially, would be cut off from a significant source of well justified tax revenues. Concomitantly, huge corporations could engage in extensive in-state activities to obtain business but would not have to pay any tax on the in-state sales secured thereby.[4]

Finally, local businesses would be subjected to a severe competitive disadvantage. For a local business would be subject to its state's sales tax, but a "foreign" business would not be.

F. West Virginia's Tax on Sales to West Virginia Customers Is Constitutional Because Armco Is a Unitary Enterprise Which Performs a Crucial Aspect of its Integrated Business Activities Inside the State

The foregoing establishes that West Virginia can tax Armco's wholesale sales to West Virginia customers because Armco engages in revenue generating in-state activities which create the very sales being taxed, and obtains benefits and protections from the state. There is

---

[4] To insure nontaxability, corporations would engage in evasive devices such as formally accepting orders in another state and having title pass elsewhere than in the buyer's state.

also an additional reason why West Virginia can tax sales to in-state customers: Armco is a unitary business enterprise with major components located in the taxing state.

The unitary nature of Armco's overall enterprise is demonstrated by the fact that Armco is a vertically integrated company. It mines coal, uses the coal to manufacture steel, uses the steel to fabricate steel products, and distributes the products to wholesalers and users. Armco's degree of vertical integration is such that its various activities are not even organized into separate corporations. Rather, the foregoing activities are carried out by a single corporation with a number of divisions.[5]

The point of the entire overall enterprise, of course, is to sell the fabricated end products. Armco makes such sales to customers located in West Virginia, a state where it engages in the coal mining that forms a basic link in the chain of vertically integrated activities that are consumated by the customer's purchase of the end product.[6] When a crucial link in the enterprise occurs in-state, the state can tax an ultimate sale to a customer who is also located in-state. For the state is doing no more than taxing the in-state consummation of a unitary series of activities that in important part occurred within the state. *Container Corporation of America v. Franchise Tax Board*, —— U.S. ——, 103 S. Ct. 2933, 2940, 2941 (1983) (A state may tax a unitary business if "at least some part of it is conducted in the state").

---

[5] Because it is vertically integrated, Armco obtains the benefits of "an umbrella of centralized management and controlled interaction." *Exxon Corporation v. Wisconsin Department of Revenue*, 447 U.S. 207, 224 (1980).

[6] Armco's West Virginia coal mining receives the same benefits and protection from the state as do its other activities within West Virginia. That is, it receives the benefits of roads, courts, police and fire protection and so forth.

Indeed, the permissibility of taxing the in-state sales of a unitary business in these circumstances follows *a fortiori* from this Court's decision in the *Container* case. There California was permitted to levy a tax on income earned outside the state by means of activities and assets located outside the state. Here West Virginia is taxing only the receipts from sales made to customers *inside* the state, and the coal mining on which the taxation can be premised also occurred inside the state.

II. THE WEST VIRGINIA SYSTEM OF TAXATION IS FAIR AND NONDISCRIMINATORY

A. Introduction

Armco claims that the West Virginia system of taxation discriminates against interstate commerce. This is not true. The West Virginia tax system is a fair, reasonable, and nondiscriminatory one which comports with decisions of this Court. Moreover, to the extent that it may give an advantage to anyone, the advantage goes not to in-state manufacturers who sell to customers within the state, but to companies like Armco which manufacture out-of-state and sell to customers in West Virginia. If anything, therefore, the Washington system *favors* interstate commerce instead of discriminating against it.

B. Well Established Principles Govern Armco's Claim

Armco's claim of discrimination is governed by well-established principles laid down by this Court. To begin with the Court has repeatedly ruled that, in considering a claim of discrimination, a "proper analysis must take 'the whole scheme of taxation into account. . .'" *E.g.*, *Halliburton Oil Well Co. v. Reily*, 373 U.S. 64, 69 (1963) (citations omitted). This was reiterated as recently as last term, when the Court said a determination whether a tax is discriminatory "requires 'an examination of the whole tax structure of the state'." *Washington v. United States*, —— U.S. ——, 103 S.Ct. 1344, 1348 (1983).

Furthermore, when considering whether a tax is discriminatory, "equality . . . is measured in dollars and cents, not legal abstractions." *Halliburton Oil Well Co. v. Reily, supra*, 373 U.S. at 69-70. Thus, regardless of abstract contentions, a party is not the victim of prohibited discrimination when it is "*better off* than other taxpayers because [it] pay[s] less tax than anyone else in the state." *Washington v. United States, supra*, —— U.S. at ——, 103 S. Ct. at 1348 (emphasis in original).

Finally, a taxpayer cannot prevail on a claim of discrimination unless it carries "the distinct burden of showing by 'clear and cogent evidence' " that a tax is unconstitutional. *Container Corporation of America v. Franchise Tax Board, supra*, 103 S.Ct. at 2939-2940 (citations omitted). The taxpayer cannot succeed by merely "showing a fair difference of opinion which as an original matter might be decided differently." *Norton, supra*, 340 U.S. at 380.

C. The West Virginia Tax System Is Lawful Under the Foregoing Principles

Under these governing principles the West Virginia tax system is plainly constitutional. West Virginia imposes a manufacturing tax at the rate of .88 percent on goods produced in the state. It also imposes a wholesale sales tax at the far lower rate of .25 percent on tangible goods sold at wholesale to West Virginia customers. The latter tax is forgiven, however, if the goods were manufactured in the state and the manufacturing tax is paid on them.

When considered as a whole, the system does not discriminate against interstate sellers like Armco, who manufacture their goods out-of-state and sell them to West Virginia customers. Rather, on a practical dollars and cents basis, such sellers will normally pay less tax than is paid when goods are manufactured within the state.

Because the tax rate on wholesale sales is far less than the rate on in-state manufacturing, the actual tax paid on goods manufactured elsewhere but sold in West Virginia will be less than the amount paid on goods manufactured within the state unless the wholesale price of the "foreign" goods is more than 350 percent higher than the manufactured value of the "local" goods. If a product manufactured within the state has a manufactured value of $1,000, the manufacturing tax, imposed at a rate of .88 percent, will be $8.88. If the product is produced elsewhere but is sold in West Virginia, the wholesale sales tax will be less than $8.88 unless the wholesale price of the product is more than $3,500,[7] *i.e.*, is more than 350 percent of its manufactured value.

It is a rare situation, however, when the wholesale price of a product is more than 350 percent of its manufactured value. Moreover, under the statute it will often be impossible for such a case to arise, and it appears to be impossible with regard to the Armco sales at issue here. For the statute provides that the manufactured value of a product is "the gross proceeds derived from the sale thereof by the manufacturer." W.Va. Code § 11-13-2b. Such sales may themselves be wholesale sales, as Armco's are here, and in such instances the manufactured value and the wholesale sales price are one and the same.

Thus, far from discriminating against an interstate seller such as Armco, on its face the West Virginia statute favors such a seller on a dollars and cents basis. For such seller will generally pay less tax to the state than would be paid if goods were manufactured within West Virginia. Nor has Armco even *alleged* (let alone tried to prove by clear and cogent evidence) that the actual facts of the present case are any different than this. That is, Armco has not even alleged that it pays

---

[7] .25 times 3500 equals $8.75.

more tax to the state under the .25 percent wholesale tax rate than would be paid under the .88 percent manufacturing rate.

Nor has Armco even alleged, let alone tried to prove, that in actual fact it suffers discrimination because of the combined effect of the West Virginia wholesale sales tax plus a manufacturing tax in Ohio, where it produces its goods. Armco has not claimed that, because of the West Virginia wholesale sales tax plus an Ohio tax, it in fact pays a greater combined sum in manufacturing and wholesale taxes than would be paid if its goods were manufactured in West Virginia. Rather than even claim this to be the actual fact, it simply presents hypothetical and speculative possibilities concerning what the situation *might* be *if* Ohio had a tax. But hypothetical and speculative possibilities, with no apparent basis in fact, are not "clear and cogent evidence" and do not meet the taxpayer's "distinct burden" of showing by evidence that a tax is unconstitutional. Were the situation otherwise, the essential taxing power of states which are hard pressed financially would be crippled by hypothetical arguments lacking any factual basis.[8]

---

[8] We note that, just as Armco's claim of discrimination is hypothetical and without factual basis, so too is any possible claim of lack of apportionment. For there is neither allegation nor proof that any state other than West Virginia is taxing Armco's wholesale sales to West Virginia customers. Allegation and proof are missing though the taxpayer, of course, has the burden of establishing failure of apportionment. *Standard Pressed Steel Co. v. Washington Dept. of Revenue, supra*, 419 U.S. at 563. In any event, a claim of lack of apportionment would be specious because West Virginia's tax is " 'apportioned exactly to the activities taxed'," *i.e.*, to sales to customers in West Virginia. *Ibid.*, quoting *Gwin, White & Prince v. Henneford, supra*, 305 U.S. at 440.

We also note that, if situations were to arise in which *actual* problems of discrimination or lack of apportionment were presented by the combined effects of taxes imposed by two or more states, the problem could be solved in a less drastic and crippling fashion than completely overturning the state taxes. One less drastic solution would be for one or more of the involved states to forgive or remit a portion of the tax otherwise owing.

D. The Validity of West Virginia's Tax System Is Supported by Decisions of This Court

Finally, the valid and nondiscriminatory nature of the West Virginia tax system is demonstrated by prior decisions of this Court upholding similar systems of taxation. In *Caskey Baking Co. v. Virginia*, 313 U.S. 117 (1941), the State of Virginia imposed a license tax on each vehicle used in the business of selling goods or merchandise in the State. However, the license tax did not apply to local manufacturers who paid a tax on their capital, or to local distributors with a fixed place of business who paid a state tax on their purchases.

The tax was challenged as discriminatory by an out-of-state producer, but was upheld by this Court. The Court pointed out that the license tax was a component of a comprehensive scheme of taxation under which the parties exempted from the license tax paid other taxes to the state. The Court also noted that, if out-of-State sellers were not subject to the tax, they would be the only sellers in Virginia to escape some form of taxation. 313 U.S. at 120-121.

The same factors are present here. West Virginia has an overall scheme of taxation; parties exempted from the wholesale sales tax pay other taxes; and if out-of-state manufacturers are not subject to the wholesale tax on sales to West Virginia customers, then such manufacturers will escape taxation in the state while in-state manufacturers will be required to pay tax.

Alaska v. Arctic Maid, 366 U.S. 199 (1961), also supports the West Virginia tax. In that case the state imposed a four percent tax when fish were "obtained for processing through freezing." 366 U.S. at 200. Owners of freezer ships which caught Alaskan fish and took them to the state of Washington for canning claimed the tax was discriminatory. This Court rejected the claim of discrimination because local Alaskan canneries

paid a different tax of six percent on fish which they obtained for canning. The Court also said that, if there was any discrimination, it was in favor of the freezer ships because the tax on their fish was less than the tax on fish obtained by local canners.

Again, the same factors exist in the present case. For companies which manufacture in West Virginia pay a different tax than out-of-state manufacturers such as Armco, and the tax paid by the local producers is higher than that paid by the "foreign" producers.

CONCLUSION

For the foregoing reasons, the decision of the court below should be affirmed.

Respectfully submitted,

LAWRENCE R. VELVEL
Chief Counsel
ELAINE D. KAPLAN
Attorney
State and Local Legal Center
444 North Capitol Street, NW
Suite 349
Washington, D.C. 20001
(202) 638-1445

STEFAN F. TUCKER
JOSEPH G. HOWE, III
TUCKER, FLYER, SANGER & LEWIS
1730 Massachusetts Avenue, NW
Washington, D.C. 20036
Counsel for the *Amici Curiae*

Dated: February 1984